

Legislative Council Panel on Commerce and Industry
The Applied Research Fund

INTRODUCTION

This information paper provides an update on the financial position of the Applied Research Fund (ARF) for the period of 1 March 2003 to 31 May 2003.

BACKGROUND

2. The ARF is a government owned venture capital fund of \$750 million set up in 1993 to provide funding support to technology ventures and research and development projects that have commercial potential. The longer term aim is to increase the technology capability and to enhance the competitiveness of local industry, thereby promoting high value added economic development in Hong Kong. The ARF is controlled and administered by the Applied Research Council (ARC), a company wholly owned by the Government and formed specifically for this role.

3. As we started to engage private sector venture capital firms to be the ARF's fund managers in November 1998, the investments of the ARC fall into two categories: those which were processed by the then Industry Department (ID) and funded before the appointment of private sector fund managers, and those which were identified by fund managers and funded after the appointment of fund managers.

4. We briefed Members on the application and management of the ARF at the Panel meeting on 11 December 2000¹, and undertook to provide quarterly written reports on the progress of the ARF. This paper provides another update since the one submitted in March 2003 and is the ninth quarterly report since then². Earlier on in February 2003, the Administration also briefed Members on the review of the role and future of the ARF.³

¹ Ref. : LC Paper No. CB(1)276/00-01(02).

² Previous papers of the same series are LC Paper Nos. CB(1)989/00-01, CB(1)1834/00-01, CB(1)939/01-02, CB(1)1232/01-02(04), CB(1)2185/01-02, CB(1)24/02-03, CB(1)582/02-03 and CB(1)1415/02-03.

³ Panel paper CB(1)844/02-03(04) discussed by the Panel on 10 February 2003 refers.

LATEST DEVELOPMENT

I. Projects processed by the then ID

5. The ARC has approved 27 projects in this category with a total amount of \$97 million. We have reported in the last update that among these 27 projects, we have exited from 18 projects in the forms of loans fully repaid (7 cases), loans written off (7 cases), equities sold at nominal value (3 cases) and company dissolved (1 case). As a result, we have written off a total of some \$29.7 million or 31% of the total approved amount.

6. Among the remaining nine projects, we have provided support in the form of equity injection for two cases and in the form of loans for the other seven cases. Details on the progress of these nine cases are reported in paragraphs 7 to 9 below.

Equity Cases

7. During this reporting period, we have sold the shares in one company at net asset value. As a result, we have written off an additional \$0.75 million or 0.8% of the total approved amount. We are still holding shares in one company.

Loan Cases

8. Among the seven loan cases, two companies were repaying the loan, one of which started payment during the reporting period. The companies of another two cases have indicated difficulties in repaying the loan in accordance with their repayment schedules. We have been discussing with them on how to resolve the matters.

9. We have taken legal actions for the remaining three cases and among which, we obtained favourable court rulings in two cases. Among these two cases, we have reached settlement agreement with the guarantors of one of the loan cases during the reporting period. As a result, we have written off an additional \$0.3 million or 0.3% of the total approved amount. For the other case, we were continuing with the appropriate course of enforcement actions and negotiation on settlement offers. The legal proceedings of the remaining case were still on-going.

II. Projects funded through fund managers

10. Since the last update, the ARC has approved two new investments and one follow-on investment totalling \$23.65 million in the information technology, electronics and environmental technology sectors. As of end May 2003, the ARF has supported a total of 24 projects through fund managers with approved funding of \$387 million. During this reporting period, we have sold the shares in one investee company at nominal value. Details of the 18 active investments⁴ are at **Annex A**. The sectoral distribution of these funded projects is at **Annex B**.

11. The latest valuation as at 31 March 2003 of all the investments managed by our fund managers⁵ stood at 61% of the total investments at cost⁶. The main reason for the below cost valuation remains to be that our fund managers have continued to be prudent in the valuation in view of the financial difficulties confronting some investee companies and the general unfavourable investment climate for technology businesses.

ADVICE SOUGHT

12. Members are invited to note this paper.

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⁴ We reported in the paper of December 2000 (Ref: LC Paper No. CB(1)276/00-01(02)) that two investments had been written off, in the update of January 2002 (Ref: LC Paper No. CB(1)939/01-02) that one investee company had been wound up, in the update of June 2002 (Ref: LC Paper No. CB(1)2185/01-02) that one investee company is in the process of liquidation, and in the update of October 2002 (Ref: LC Paper No. CB(1)24/02-03) that another investee company is in the process of liquidation. We have sold the shares in another company as covered in paragraph 10 of this paper. This means a loss of a total of \$75.39 million or 19.5% of the approved funding. Hence, a total of 18 investments are active.

⁵ We reported in the update of October 2002 (Ref: LC Paper No. CB(1)24/02-03) that the investments previously managed by AsiaTech Ventures Limited have been managed by the ARC directly since 3 May 2002.

⁶ The valuations of investee companies are provided by fund managers on the basis of the evaluation of individual investee company in its latest round of financing or as evaluated by the fund managers. If there is no additional round of financing after ARF's investment, our equity will be valued at our investment cost.

**List of Active Investments Approved by the Applied Research Council
after the Engagement of Fund Managers in November 1998
(Position as at end May 2003)**

Information Technology

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
ecVision Ltd.	Walden Technology Management (HK) Ltd.	Business-to-business e-commerce software and services	27.24
LECCO Technology Ltd.	Walden Technology Management (HK) Ltd.	Software tools	24.59
Wisers Information Ltd.	Walden Technology Management (HK) Ltd.	Electronic aggregation and distribution of Chinese language-based content	38.20
InfoTalk Corporation Ltd.	Walden Technology Management (HK) Ltd.	Automatic speech recognition	24.15
WebPro Ltd.	Walden Technology Management (HK) Ltd.	Internet and e-commerce technologies for the Asian electronics components industry (internet & e-commerce)	15.60
iASPEC Technologies Inc. (formerly Uni-tech Systems Engineering Ltd.)*	–	System integration, application hosting services	15.55

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
i-Security Solutions Ltd.	Walden Technology Management (HK) Ltd.	To develop and market encryption and authentication tools to facilitate e-commerce functions	10.82
QuotePower Information Ltd.*	–	Provision of online financial information and real-time electronic trading	8.00
Emsoft Limited	Softech Investment Management Co. Ltd.	To develop software applications and operating systems for embedded devices based on the Linux platform	7.80
Total			171.95

Biotechnology

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
Plasmagene Biosciences Limited	Softech Investment Management Co. Ltd.	To research and develop non-invasive techniques for detection of prenatal and cancerous diseases based on proprietary and licensed technologies	11.70
Total			11.70

Telecommunications

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
Wafer Systems Limited	HSBC Private Equity Technology (Asia) Ltd.	Network integration	46.70
Continuous Technologies International Ltd.*	–	Computer telephony applications	18.14
Unitech Networks Ltd.	Walden Technology Management (HK) Ltd.	Internet/Intranet system integrator	11.63
CommVerge Solutions Ltd.	Walden Technology Management (HK) Ltd.	Telecom system integration	7.80
iMagic Infomedia Technology Limited	Softech Investment Management Co. Ltd.	Development of computerized public payphones and kiosks	5.00
Total			89.27

Electronics

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
NSM Holdings Ltd.*	–	Original design manufacturer of telecom equipment	15.58
Dragonchip Limited	Softech Investment Management Co. Ltd.	To design IC chips with embedded Flash memory for consumer electronics applications	17.94
Total			33.52

Environmental Technology

Investee Company	Fund Manager	Technology Area	Funding Approved (HK\$m)
Enpro Environmental Technologies Co. Ltd.	Softech Investment Management Co. Ltd.	Provision of noise, air and wastewater pollution solutions	5.00
Total			5.00

* Investments under the custody of the ARC

**Sectoral Distribution of Active Projects
Approved by the Applied Research Council
after the Engagement of Fund Managers
(Position as at end May 2003)**

